

STATE OF RHODE ISLAND AND PROVIDENCE PLANTATIONS
PUBLIC UTILITIES COMMISSION

IN RE: NARRAGANSETT ELECTRIC COMPANY :
PROPOSED RATE REDUCTIONS TO STANDARD : DOCKET NO. 3479
OFFER RATE, TRANSITION CHARGE AND :
TRANSMISSION ADJUSTMENT FACTOR :

REPORT AND ORDER

I. BACKGROUND

The Utility Restructuring Act of 1996 (“URA”) requires each electric distribution company to arrange with wholesale power suppliers for a standard power supply offer to sell electricity to all customers at a stipulated rate. Pursuant to the URA, Narragansett Electric Company (“Narragansett” or “Company”) entered into wholesale Standard Offer supply contracts with the following prices:

<u>Calendar Year</u>	<u>Price per kWh</u>
2003	4.7 cents
2004	5.1 cents
2005	5.5 cents
2006	5.9 cents
2007	6.3 cents
2008	6.7 cents
2009	7.1 cents

The wholesale Standard Offer supply contracts also provide for increases in the price per kilowatt-hour (“kWh”) of wholesale power supplied to Narragansett in the event fuel prices increase above certain levels. To the extent that the total cost of the wholesale power supply to Narragansett, including fuel charges, exceeds retail Standard Offer Service (“SOS”) and Last Resort Service (“LRS”) revenues, the under-collection is recoverable from Narragansett’s customers through the annual reconciliation provisions of Narragansett’s Standard Offer Adjustment Provision. Likewise, to the extent

Narragansett collects more than its total cost of providing SOS, the ratepayers are entitled to recoup the benefit, with interest. Furthermore, Narragansett's transmission and transition charges are fully reconciling on an annual basis, the transition charges through an adjustment based on the annual reconciliation of wholesale power contract termination charges ("CTC") filed by National Grid, and the transmission charges through a change in Narragansett's transmission adjustment factor ("TAF").

II. NARRAGANSETT

On November 18, 2002, Narragansett filed with the Rhode Island Public Utilities Commission ("Commission") its annual reconciliation filing with respect to SOS, transition and transmission rates. The filing included: a request not to adjust the retail SOS rate from the present rate of 4.662 cents per kWh; a proposed increase in the transition rate from the present rate of .874 cents per kWh to .944 cents per kWh; and a proposed increase the transmission adjustment factor from the present rate of .063 cents per kWh to .107 cents per kWh. The result for a typical residential customer using 500 kWh of service would be an increase of 1.1% equal to \$0.60 per month. Therefore, the average monthly residential bill would increase from \$54.24 to \$54.84.¹ In support of the proposed rates, Narragansett presented the pre-filed testimony of Jeanne A. Lloyd, Principal Financial Analyst from National Grid USA Service Company, Michael J. Hager, Director, Energy Supply - NE for National Grid USA Service Company, and Anne M. Rodrigues, Senior Analyst in Transmission Rates and Forecasting for New England Power Company.

¹ Narragansett Ex. 1A, Pre-filed testimony of Jeanne A. Lloyd, pp. 3-4, Exhibit JAL-11, p. 1.

A. Standard Offer Service

In his pre-filed testimony, Michael Hager explained that Narragansett has wholesale power supply contracts with several non-affiliated generators to serve the retail SOS load within its pre-merger (“Narragansett zone”) and post-merger (both “Narragansett zone” and “EUA zone”) service territories. All of these wholesale SOS supply contracts run through December 31, 2009.² Mr. Hager explained that Narragansett’s SOS supply contracts contain two price components – a base price and a fuel index adjustment provision. According to Mr. Hager, the fuel index adjustment provides for additional payments (“fuel index payments”) to be made to the SOS suppliers in the event of substantial increases in the market price of No. 6 residual fuel and natural gas. The price is based on a comparison of six-month (“EUA zone”) and twelve-month (“Narragansett zone”) rolling average of oil and gas prices to a current trigger price. In order to determine the extent of any fuel index payments for the period January 2003 through December 2004, Mr. Hager based the fuel index adjustment calculations on future gas and crude oil projections. In performing his calculations, he used the average gas and crude oil prices as reported in the Wall Street Journal on October 28, 29, and 30, 2002. Based on the numbers examined, Mr. Hager determined that Narragansett will have to make fuel index payments of .333 cents per kWh in the pre-merger Narragansett zone and .353 cents per kWh for the period January 2003 through December 2003.³ Thereafter, Mr. Hager did not foresee the need for further fuel

² Narragansett Ex. 1B, Pre-filed testimony of Michael Hager, pp. 3-4.

³ Narragansett Ex. 1B, p. 6.

Addressing fuel index payments, Ms. Lloyd testified that during the reconciliation period October 2001 through September 2002, Narragansett incurred approximately \$25.2 million in fuel index payments. Of this amount, \$719,000 was incurred in August and September 2002, and was unexpected at the time of Narragansett's 2002 Reconciliation filing in Docket No. 3402. As a result, the current balance in the SOS account is an over-recovery of approximately \$29.3 million, and is designed to offset the under-recovery that will occur in 2004 due to the difference between the contract rate and the averaged SOS rate. However, due to the fuel index payments of \$719,000, this over-recovery is less than that which was projected by Narragansett in Docket No. 3402.⁷ Ms. Lloyd explained, that while the current over-recovery will be applied to offset the 2004 under-recovery, the forecasted fuel index payments for the period October 2002 through December 2003 are expected to cause a total under-recovery of approximately \$23.6 million through December 2004.⁸ In order to mitigate the impact of the fuel index payments, Narragansett proposes to utilize the \$20 million lump sum payment received from a supplier of SOS in December 2001 and the \$665,394 of last resort service ("LRS") over-recovery.⁹ Narragansett asserted that use of the over-recovery in the LRS account to offset the fuel index payments is consistent with past Commission policy.¹⁰

Narragansett argued that the circumstances fell within the Commission's past practice because, like in the previous cases, the current LRS over-recovery, incurred for the period October 2001 through September 2002, is due in part from out-of-period

⁷ Id. at 20.

⁸ Id. at 20-22.

⁹ Id. at 25-26.

¹⁰ Id. at 26-27. See Order No. 16635 (issued June 13, 2001) (allowing a Standard Offer adjustment factor to be applied to all kWh deliveries to collect under recoveries from both the SOS and LRS accounts) and Order No. 16916 (issued February 15, 2002) (allowing a SOS over-recovery be used to offset the LRS under-recovery incurred during the same period).

adjustments to wholesale expenses. Ms. Lloyd explained that many of the customers who had been taking LRS in the months to which the adjustments apply are now taking service from competitive suppliers.¹¹

B. \$20 million Credit

Ms. Lloyd noted that in Docket No. 3402, despite the fact that Narragansett did not expect fuel index payments to be necessary after March 2002, it had proposed to retain a \$20 million payment received from a SOS supplier in 2001 for the purposes of hedging against unexpected increases in fuel prices that could trigger fuel index payments to SOS suppliers. The Commission approved the request and had ordered the money to be held in an interest bearing account for the benefit of ratepayers. The Commission indicated that it would address the disbursement of funds “in the near future.”¹² According to Ms. Lloyd, the balance in the account as of December 31, 2002 is approximately \$21.2 million.¹³ Therefore, Narragansett proposed continuing to hold the money in an interest bearing account to be used when the balance in the SOS account is no longer sufficient to cover fuel index payments.¹⁴

C. Transition Charge

In her pre-filed testimony, Ms. Lloyd explained that the transition charge is intended to recover the contract termination charge (“CTC”) that was billed to Narragansett by its affiliated supplier, New England Power (“NEP”), when NEP released Narragansett from the all-requirements contract whereby Narragansett had contracted to

¹¹ Id. at 26-27.

¹² Id. at 23, Order No. 16916 (issued February 15, 2002).

¹³ Narr. Ex. 1A, p. 24.

¹⁴ Id. at 24-25.

buy all of the power required to serve Narragansett's customer load.¹⁵ The Non-Bypassable Transition Charge Adjustment Provision in Narragansett's retail service tariff was established in the merger agreement between Narragansett, Newport Electric Company and Blackstone Valley Electric Company.¹⁶

Narragansett reconciles transition revenues on an annual basis in accordance with the requirements of the Non-Bypassable Transition Charge Adjustment Provision, which requires an annual reconciliation of Narragansett's total CTC expense against Narragansett's total revenue from the Transition Charge. Any over or under-collection is to be refunded to or collected from customers, with interest. Ms. Lloyd indicated that the current transition rate produced an over-recovery of approximately \$1.1 million for the period October 1, 2001 through September 30, 2002.¹⁷ In order to refund the over-collection in the 2002 transition charge reconciliation, Narragansett proposed to reduce the 2003 weighted average Transition Charge of .959 cents per kWh by a credit factor of .015 cents per kWh, producing a net transition charge of .944 cents per kWh.¹⁸

D. Transmission Rate

In her pre-filed testimony, Ms. Lloyd outlined the four components of Narragansett's proposed reduction in the Transmission Adjustment Factor: (1) a decrease of .069 cents per kWh to represent a decrease in forecasted transmission costs for 2002; (2) an increase of .123 cents per kWh to eliminate the twelve-month transmission reconciliation factor from 2002; and (4) a decrease of .010 cents per kWh to refund a

¹⁵ Id. at 5-6.

¹⁶ Id. at 6-7, See Order No. 16200 (issued March 24, 2000).

¹⁷ Id. at 9-10.

¹⁸ Id. at 9-11. The weighted average transition charge is based on a formula comparing the transition charges of the Narragansett zone and the EUA zone. Id. at 6-8.

\$.733 million over-recovery from the period October 2001 through September 2002.¹⁹ The net result was a proposed increase of .044 cents per kWh, increasing the Transmission Adjustment Factor from .063 cents per kWh to .107 cents per kWh.²⁰

Narragansett forecasted total transmission costs for 2003 of approximately \$38.6 million, resulting in a unit cost of 0.514 cents per kWh for 2003, or .069 cents less than the 2002 average transmission expense of .583 cents per kWh.²¹ Ms. Lloyd explained that, as shown in Ms. Rodrigues' testimony, under current market rules, transmission rules include congestion costs and reliability must run ("RMR") costs. However, with the implementations of SMD, congestion costs will no longer be included in transmission charges. Therefore, Narragansett's forecasted transmission costs only include congestion and RMR costs for the period January 1 through March 1, 2003 (the anticipated implementation date of SMD).²²

Narragansett reported a \$6.8 million transmission revenue over-recovery as of September 30, 2002. Ms. Lloyd noted that in accordance with the Commission's Orders in Dockets No. 3031 and No. 3402, Narragansett has continued to defer recovery of certain disputed uplift costs pending the outcome of an ongoing dispute with two of its suppliers. Narragansett proposed to continue to retain \$5.1 million of the transmission over-recovery, representing disputed ISO Tariff charges, as a deferred line item pending resolution of disputed ISO Tariff charges for the years 1999, 2000, 2001. Narragansett also proposed to hold an additional \$840,000 to cover disputed ISO Tariff charges for the period October 2001 through September 2002. Narragansett indicated that it expected a

¹⁹ Id. at 11-12.

²⁰ Id. at 11.

²¹ Id. at 13.

²² Id. at 13, Narragansett Exhibit 1C (Testimony of Anne M. Roderigues), pp. 8, 10-12.

resolution of the matter within the next year. In the event arbitration is successful, Narragansett would then refund a total of \$6.1 million to customers. If, however, arbitration is unsuccessful, the Commission would have the opportunity to rule on the recovery of the disputed ISO Tariff expenses by Narragansett.²³ If recovery were allowed by the Commission, Narragansett would be able to recover those costs without raising rates.²⁴ Therefore, of the entire transmission over-recovery of \$6.8 million, Narragansett proposes refunding only approximately \$733,000 at this time.²⁵

In her pre-filed testimony, Ms. Anne Rodrigues explained that since January 1, 1998, Narragansett has been taking transmission services on behalf of its entire customer base under two open access transmission tariffs approved by FERC. Under ISO-NE's FERC Electric Tariff No. 1, ISO-NE provides Scheduling System Control and Dispatch, Energy Administration Service, and Reliability Administration Service. In addition to these charges, Narragansett is charged certain energy uplift charges which are currently under dispute between Narragansett and its Standard Offer power suppliers and, therefore, are being deferred pending the outcome of the disputes.²⁶

Ms. Rodrigues estimated Narragansett's total transmission and ISO-NE Tariff expenses for 2003 to be approximately \$38.6 million, a 9.9% decrease from the transmission charges collected in 2002, due to a reduction in congestion and energy uplift estimates over the prior estimate. She explained that her estimate included Narragansett's charges under NEP Tariff 9, NEPOOL's FERC Tariff No. 1, and charges

²³ Narragansett Exhibit 1A, pp. 14-17.

²⁴ Id.

²⁵ Id. at 16.

²⁶ Narragansett Ex. 1C, Pre-filed testimony of Anne M. Rodrigues, pp. 2-4, 8. As noted in Ms. Lloyd's testimony, the current deferred ISO Tariff expenses through September 2002 total approximately \$6.1 million.

for congestion costs and charges under ISO-NE's tariff. In estimating Narragansett's ISO-NE expenses, Ms. Rodrigues used ISO-NE's actual charges to Narragansett for the period September 2001 through August 2002 and adjusted that figure by an inflationary factor. The major increases in the estimates of Narragansett's ISO-NE charges between 2002 and 2003 are due to payroll, depreciation expense on 2003 assets and costs associated with Regional Transmission Organization activity. Similarly, estimates for NEP Tariff 9 charges were based on NEP's actual expenses from September 2001 through August 2002, with a \$2.4 million increase to reflect additional costs associated with forecasted capital additions anticipated during the next rate period.²⁷

The estimated NEPOOL tariff charges for 2002 were based on current tariff rates, with adjustments for an estimated annual increase to become effective June 1, 2003. Ms. Rodrigues' estimate included \$9.1 million in charges for certain Reactive power charges and \$4.9 million for Black Start service.²⁸

Ms. Rodrigues explained that congestion costs and reliability must run ("RMR") costs have been included in her forecasts through February 28, 2003 in anticipation of the commencement of SMD, when congestion costs and RMR will no longer be socialized among those in the New England region, but will be charged to the region requiring the services.²⁹

III. DIVISION

In response, on December 10, 2002, the Division of Public Utilities and Carriers ("Division") submitted the pre-filed testimony of its expert, Dr. John Stutz of the Tellus Institute, prepared after he reviewed the filing made by Narragansett. Dr. Stutz indicated

²⁷ Id. at 8, 11-12.

²⁸ Id. at 9.

that the Division supported the Standard Offer rate proposals by Narragansett, specifically those designed to provide stabilization against rising fuel prices but that, regarding the TAF, the Division had its own proposal.³⁰

Specifically, Dr. Stutz recommended that the Commission approve Narragansett's proposal to retain the \$20 million supplier payment and to utilize the \$665,394 LRS over-recovery to offset costs due to fuel index payments associated with SOS.³¹ However, with regard to the proposal to retain \$6.1 million of the transmission over-recovery, Dr. Stutz recommended the Commission order Narragansett to refund at least \$4 million of the \$6.8 million transmission over-recovery to avoid the proposed increase in the TAF.³²

Dr. Stutz noted that there are two significant differences between the Company's SOS proposals and its TAF proposal. First, the SOS proposals are designed to offset costs definitively recoverable from ratepayers, namely fuel index charges that Narragansett can reasonably expect to incur through September 2004. Alternatively, the TAF proposal is based on disputed costs which for which Narragansett may or may not be liable and which may or may not be recoverable from ratepayers. Second, while the SOS proposals do not result in a change in the SOS charge to ratepayers, the TAF proposal results in an increase in the TAF which could otherwise be avoided.³³ Therefore, with regard to the TAF proposal, Dr. Stutz recommended the Commission

²⁹ Id. at 9-10.

³⁰ Division Exhibit 1 (Pre-Filed Testimony of Dr. John Stutz), 3.

³¹ Id. at 2 (emphasis added).

³² Id.

³³ Id. at 4-5. Dr. Stutz noted that Narragansett's SOS proposals represent a continuation of the Commission's policy in Docket No. 3402, namely, to provide rate stability for customers through 2004. Id. at 5.

allow Narragansett to retain only about \$2.8 million of the transmission over-recovery in order to avoid an increase in the TAF.³⁴

IV. HEARING

A public hearing was held at the Commission's offices, 89 Jefferson Boulevard, Warwick, Rhode Island, on December 12, 2002.³⁵ The following appearances were entered:

FOR NARRAGANSETT:	Terry L. Schwennesen, Esq.
FOR DIVISON:	Paul J. Roberti, Esq. Assistant Attorney General
FOR COMMISSION:	Cynthia G. Wilson, Esq. Senior Legal Counsel

B. Narragansett's Testimony

At the hearing, Mr. Hager, Ms. Lloyd and Ms. Rodrigues testified on behalf of Narragansett. Ms. Lloyd made some changes to her pre-filed testimony. She indicated that when the filing was made, she had based her transition charge calculations on estimates. However, she was not proposing a change in the filed proposed transition rate.³⁶ Ms. Lloyd also testified that she had prepared an exhibit that calculates rates based on Dr. Stutz's recommendations regarding the TAF.³⁷ She indicated that Narragansett had no objection to implementing rates that would result from Dr. Stutz's recommendation to keep the TAF stable.³⁸ Under this proposal, the result for a typical

³⁴ Id. at 6.

³⁵ The hearing was originally noticed for December 11, 2002. The Commission opened the proceedings on that day for public comment. No members of the public appeared.

³⁶ Tr. 12/12/02, p. 9. The re-calculation increased the transition factor of .944 cents per kWh to .945 cents per kWh. Ms. Lloyd indicated that in her opinion, the difference was relatively insignificant and did not warrant a change in the proposed rate. Id.

³⁷ Id. at 11. Narragansett Exhibit 2.

³⁸ Tr. 12/12/02, p. 11.

residential customer using 500 kWh of service would be an increase of .7% equal to \$.37. Therefore, the average monthly residential bill would increase from \$54.24 to \$54.61.³⁹

1. Standard Offer Service

a. Fuel Index Payments

Ms. Lloyd and Mr. Hager testified that it is possible that fuel prices could rise enough to trigger the fuel index adjustment provisions of the SOS supply contracts for a longer period of time than was estimated in 2001. In fact, after a review of oil and natural gas futures prices as of December 11, 2002, Mr. Hager testified that fuel index payments could double over the estimated \$23.4 million that Narragansett originally included in its filing.⁴⁰ Therefore, Ms. Lloyd conceded that Narragansett may require a SOS base rate increase prior to the end of 2004.⁴¹

b. Reconciliation Account Off-Set

Narragansett's filing proposed to retain the LRS over-collection for the period October 2001 through September 2002 to offset the anticipated fuel index payments. Ms. Lloyd explained that, like the basis for the offset that was previously allowed between the SOS account and LRS account in Docket No. 3402, the over-collection was due in large part to out-of-period adjustments that were related to non-residential customers who were taking LRS in a prior period. Ms. Lloyd noted that the timing issue is created by the NEPOOL settlement process. The monthly true-up procedure reconciles monthly estimates with actual charges. Payments have been made to Narragansett as late as up to six months after a prior period. Those customers no longer taking LRS would be administratively difficult to identify (if they are still customers of Narragansett at all) for

³⁹ Narragansett Ex. 2, Exhibit JAL-11, REVISED, p. 1 of 23.

⁴⁰ Tr. 12/12/02, pp. 22-26.

purposes of a refund.⁴² Furthermore the majority of the ratepayers currently taking LRS are residential customers who are charged the SOS rate, not the non-residential LRS rate which is higher.⁴³

c. \$20 million Credit

Regarding the \$20 million credit received by Narragansett from NEP in connection with the transfer of the SOS supply contract from NEP to another supplier, the Commission allowed Narragansett to retain the credit in an interest bearing account as a cushion against additional fuel index payments. Narragansett proposed to continue to hold the \$20 million credit for use in 2004, when the SOS over-recovery is expected to be depleted due to additional fuel index payments. In response to questioning from the Bench, Ms. Lloyd indicated that Narragansett could have two reconciliations in the SOS reconciliation. One would be to reconcile the base SOS expenses against retail revenues and apply the \$20 million credit in 2004, and the other would apply the \$20 million credit to fuel index payments as incurred. Mr. Hager estimated that the alternative of applying the credit to the fuel index payments on a monthly basis rather than in 2004 would have the same effect to the ratepayers. Ms. Lloyd expressed concern that because of the methodology used in applying interest, ratepayers could realize less benefit from the alternate proposal.⁴⁴

⁴¹ Id. at 27-28.

⁴² Id. at 39-41.

⁴³ Id. at 42-43.

⁴⁴ Id. at 29-35. The calculation of the alternate proposal was requested as a record request and on December 17, 2002, Narragansett filed the response. Ms. Lloyd's conclusion was that the alternate proposal would provide a slight advantage to ratepayers and therefore, Narragansett had no objection to reconciling the SOS account in this manner. Narragansett Response to Record Request 1.

2. Transition Charge

Ms. Schwenessen explained that Narragansett's transition charge reflects the CTC charged to it by NEP under a FERC-approved settlement⁴⁵ to which Narragansett, the Commission and Division were parties. CTC charges, which are reconciled annually by NEP, can be challenged through a dispute resolution process under the settlement. Currently, there are unresolved issues between NEP and the non-utility parties (Commission and Division) to the settlement relating to NEP's CTC reconciliation.⁴⁶

In order to address the increase in the transition charge from the previous period, Narragansett presented Michael LaFlamme, Manager of Regulatory Support for National Grid, who is primarily responsible for developing the CTC reconciliations. He testified that fewer credits were being flowed through the 2003 projected rates than were flowed through the 2002 projected rates, due to some one-time divestiture-related credits regarding Millstone 3 proceeds and due to actual kilowatt hour sales adjustments.⁴⁷

Mr. Roberti represented that Division consultant David Effron had reviewed that transition rate reconciliation charge and had determined it to be correctly calculated in accordance with the settlement reached in Docket No. 2930. However, Mr. Roberti confirmed that there were still outstanding issues relative to certain charges in the NEP reconciliation filing.⁴⁸ With regard to those outstanding issues, Mr. LaFlamme noted that there is an inherent one-year lag in the NEP reconciliation and furthermore, the alternative dispute process contained in the FERC settlement has no time constraint for

⁴⁵ FERC Docket No. ER97-680-000.

⁴⁶ Tr. 12/12/02, p. 6, 49-52.

⁴⁷ Id. at 48-49, 51-53.

⁴⁸ Id. at 49-51.

resolution and adjustments. Therefore, there is no risk of losing benefit because of the time delay.⁴⁹

Addressing her calculations, Ms. Lloyd explained that the proposed transition charge is based on forecasts of Narragansett's sales. There are two forecasts used in the calculation. The first is a NEP forecast that was established when Narragansett merged with Newport/BVE in 2000.⁵⁰ The second is a Narragansett forecast which is updated each year. Ms. Lloyd noted that Narragansett's more recent sales forecasts have tended to be higher than the original NEP sales forecast for each year. She explained that the Narragansett forecasts are used only to calculate the weighted average rate when considering the former Newport/BVE and the former Narragansett territories as separate retail areas for purposes of setting the retail transition rate.⁵¹ It was her understanding that the weighted average calculation would have to be performed through the rate freeze period which ends December 31, 2004.⁵²

3. Transmission Rate

On cross-examination, Ms. Lloyd indicated that she had revised the TAF in accordance with the Division's proposal to refund enough of the over-collection to avoid an increase from the 2002 TAF.⁵³ She stated that Narragansett recognizes that the over-collection represents the deferred expenses associated with ISO tariff charges that have not yet been approved by the Commission for recovery by Narragansett. Therefore,

⁴⁹ Id. at 51-52.

⁵⁰ The Merger was filed by Narragansett, Newport Electric and BVE on August 24, 1999 and approved by the Division on February 25, 2000. See Division Order No. 16186 (issued February 25, 2000). The rates for the consolidated entities were approved in Commission Docket No. 2930. See Commission Order No. 16200 (issued March 24, 2000).

⁵¹ Tr. 12/12/02, pp. 45-46.

⁵² Id. at 46-47.

⁵³ Tr. 12/12/02, p. 53, Narragansett Exhibit 2 (Exhibit JAL-4 Revised). The typical residential customer using 500 kWh per month would realize an overall monthly bill increase of 37 cents.

Narragansett has no objection to refunding whatever amount the Commission believed to be appropriate.⁵⁴ However, Ms. Rodrigues noted that if SMD does not go into effect on March 1, 2003, as currently expected, Narragansett would continue to incur congestion uplift charges and reliability charges. She estimated that Narragansett's liability would be approximately \$710,000 per month for both services.⁵⁵

Mr. Hager updated the Commission on the status of the formal dispute resolution process over the disputed ISO Tariff charges. He testified that hearings in the binding arbitration proceeding are expected in February 2003 with a decision expected in mid-2003. Narragansett has not determined whether, in the event Narragansett is unsuccessful, the Company will seek recovery from ratepayers through its annual reconciliation filing or through a separate proceeding.⁵⁶

Mr. Hager also noted that there is disagreement between Narragansett and certain energy suppliers with regard to the impact of the SMD rules with regard to allocation of responsibility for certain congestion costs under Narragansett's SOS supply contracts with those suppliers.⁵⁷ He explained that discussions are ongoing and that at least one of the disputes is expected to be resolved in early 2003.⁵⁸ Narragansett agreed to defer recovery of the costs from ratepayers until the disputes had been resolved, at which point, Narragansett would approach the Commission to request recovery through rates of any amounts it owes through rates.⁵⁹

⁵⁴ Tr. 12/12/02, p. 54.

⁵⁵ Id. at 59.

⁵⁶ Id. at 60-61. The ongoing dispute is between Narragansett and suppliers over who has responsibility for certain uplift, certain ISO tariff expenses, and further miscellaneous charges.

⁵⁷ Id. at 180.

⁵⁸ Tr. 12/12/02, pp. 61-62.

⁵⁹ Id. at 63.

Finally, Ms. Lloyd presented the Commission with the calculation of rates assuming all of the transmission over-collection was returned to customers through this reconciliation. She testified that even if the entire over-collection was returned to customers in 2003, the typical residential customer using 500 kWh per month would experience an increase in his or her overall bill of 16 cents.⁶⁰

C. Division's Testimony

The Division presented Dr. John Stutz, Vice President of the Tellus Institute, in support of its position.⁶¹ Dr. Stutz summarized his testimony, noting that he supported the Company's proposal concerning the use of the LRS over-recovery and the \$20 million as a hedge against rising fuel costs. Specifically addressing the flow-back of the transmission over-recovery, he testified that refunding all or part of it would be reasonable. He noted that a partial refund would allow Narragansett to hedge against the costs associated with the possibility that the SMD would not be implemented on March 1, 2003.⁶²

With regard to the proposal from the Bench to apply the \$20 million credit as incurred for fuel index payments or to hold it until Narragansett faces a deficit in the SOS account, Dr. Stutz testified that as long as Narragansett could show that ratepayers will not be adversely affected by one approach, either is reasonable. He did agree that public perception may be more positive if the money was being applied as currently needed

⁶⁰ Id. at 66-68, Narragansett Exhibit 4.

⁶¹ Dr. Stutz has had extensive experience with energy-related matters, particularly with regard to public utilities. Since 1977 he has appeared before Public Utility Commissions in 36 states, the District of Columbia, and three Canadian provinces. In total, he has appeared in approximately 140 utility proceedings. He has testified on a variety of topics involving planning, pricing, and regulatory policy in cases involving electric, gas, and telephone companies. Div. Ex., Schedule JS-1.

⁶² Id. at 56-58.

rather than being held for a future benefit. However, he also noted that because the SOS rate is not being increased in 2003, there may not be a strong price signal either way.⁶³

Addressing the ongoing disputes between Narragansett and its suppliers, Dr. Stutz agreed that the Company should defer the recovery of any costs found to be Narragansett's responsibility relative to SMD in the same way it has been deferring costs associated with ISO Tariff charges until such time as the Commission is presented with the opportunity to rule on the reasonableness of those charges.⁶⁴

V. COMMISSION FINDINGS

At an open meeting on December 20, 2002, the Commission considered the evidence presented and approved Narragansett's rate proposal as filed in part and denied the proposal as filed in part. Specifically, the Commission approved Narragansett's proposals with regard to the SOS rate, transition rate, and the LRS over-recovery, as just and reasonable and in the best interests of the ratepayers.

With regard to the TAF, the Commission found the Division's recommendation to return \$4.0 million of the over-recovery and to allow Narragansett to retain \$2.8 million to be just and reasonable and in the best interests of the ratepayers. The Commission notes that even if the Commission orders a refund of the entire over-recovery, customers will still realize an overall rate increase. This approach of refunding a portion of the over-recovery allows for rate stability while also providing for a hedge against transmission-related expenses in the event the implementation of SMD is delayed beyond March 1, 2003. At a potential \$700,000 monthly liability, this approach provides an additional four months of transmission rate stability for ratepayers.

⁶³ Id. at 73-78. Dr. Stutz also noted that public perception does play a role in ratemaking. Id. at 78.

⁶⁴ Id. at 62-63.

In addition, the Commission finds the Company's proposal to apply the \$20 million supplier credit to additional fuel index payments to be reasonable. However, Narragansett has demonstrated in response to Commission Record Request 1 that application of these funds on a pay-as-needed basis provides a greater benefit to ratepayers than if Narragansett held the funds until the SOS account is depleted. Therefore, the Commission finds that Narragansett is to apply the \$20 million to fuel index payments as they are incurred and to use the SOS account to cover the base price.

The Commission is aware that the averaged SOS rate put into effect at the start of 2002 with the hopes of providing three years of rate stability to customers may need to be adjusted upward due to rising fuel costs. The threat of war in the Middle East and a labor dispute in Venezuela by oil workers has helped to create a level of uncertainty that is adversely affecting the price of oil and natural gas commodities.

Accordingly, it is hereby

(17424) ORDERED:

1. Narragansett Electric Company's proposed continuation of the retail Standard Offer Service Rate of 4.662 cents per kWh is approved for service on and after January 1, 2003.
2. Narragansett Electric Company's proposed Transition Rate of .944 cents per kWh is approved to become effective for service on and after January 1, 2003.
3. Narragansett Electric Company's proposed retail Transmission Rate of .063 cents per kWh is approved to become effective for service on and after January 1, 2003.

4. Narragansett Electric Company shall apply the \$20 million credit to fuel index charges as incurred under its Standard Offer Service supply contracts.
5. Narragansett Electric Company shall apply the Last Resort Service account over-recovery for the period October 1, 2001 through September 30, 2002 to fuel index charges as incurred.
6. Narragansett Electric Company shall comply with all other findings and instructions as contained in this Report and Order.

EFFECTIVE AT WARWICK, RHODE ISLAND PURSUANT TO AN OPEN MEETING DECISION ON DECEMBER 20, 2002. WRITTEN ORDER ISSUED APRIL 11, 2003.

PUBLIC UTILITIES COMMISSION

Elia Germani, Chairman

Kate F. Racine, Commissioner

Brenda K. Gaynor, Commissioner